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SUBJECT: KALININGRAD AGRIBUSINESS FORUM: GERMAN FARMERS TO
RETAKE KOENIGSBERG?

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¶1. (SBU) SUMMARY: Kaliningrad Oblast's first international agribusiness forum intended to stimulate foreign investment drew a respectable, German-dominated audience of foreign farmers and processors. The oblast minister of agriculture conceded that openly inviting German farmers to come to the oblast 60 years after their compatriots were driven out could draw criticism from other Russian politicians, but with over 40 percent of Kaliningrad Oblast's agricultural land idle and investment languishing, it is a risk worth taking. END SUMMARY.

¶2. (U) Kaliningrad Oblast's government hosted its first international forum to attract foreign investors in production agriculture and agribusiness May 17. The forum was opened by Governor Georgiy Boos, followed by Vice Governor Yuriy Shalimov, Minister of Economy Feliks Lapin, and Minister of Agriculture Andrey Romanov, each of whom opened his remarks with the words, "Kaliningrad Oblast is an integral part of the Russian Federation." Each extolled the virtues of investing in Kaliningrad based on its location and tax breaks, paving the way for topical presentations by two bankers (local heads of Sberbank and Rosselkhozbank), the head of the oblast tax directorate, local chamber of commerce, and testimonials from successful local and foreign investors in food processing, including Croatian-owned Produkty Pitaniya and Lithuanian-owned Vicunai-Rus. An added attraction was presence all day of Lithuanian Minister of Agriculture and former Prime Minister Kasimiera Prunskiene.

¶3. (SBU) Two highlights were presentations by German academics, Prof. Gerd Graef, a private consultant, and Prof. Holger Klink of the University of Kiel, whom the oblast had commissioned to spend six months studying Kaliningrad Oblast agriculture and then to report on its potential for revival in the event German farmers could be enticed to invest both capital and know-how. The professors noted that climatic and soil conditions of Kaliningrad are not dissimilar to those of northern Germany, though with a somewhat shorter growing season. These excellent lectures were offset somewhat by a lengthy diatribe by German Ministry of Agriculture specialist Martin Struck, who opened with complaints about radar-toting Russian traffic police and undisciplined pedestrians, to the amusement of the audience, then concluded with a sales pitch for German technical assistance. Another low was the boastful, in-your-face presentation by Konstantin Khaypov of Inteko Agro, agricultural subsidiary of the construction firm owned by Moscow Mayor Yuriy Luzhkov's wife, Yelena Baturina.

Khaypov openly challenged Prunskiene, saying within a few years Inteko's investment in Kaliningrad Oblast would result in Inteko alone exporting more to Lithuania than Lithuania currently exports to all of Russia. He offered naught but high expectations, though, as Inteko has yet actually to accomplish much in Kaliningrad.

AGRICULTURAL CONDITIONS IN KALININGRAD

¶4. (U) Oblast Agriculture Minister Romanov reported that out of a total of 723,000 hectares of agricultural land, over 40 percent is unused and has been essentially abandoned. In another ten years, he said, it will be overgrown to the point that reclamation will be prohibitively expensive, so now is the time for investors to come in and start farming. He noted that rapeseed production (for export to Germany to be processed) is on the rise, and that while beef and pork production continues to contract, production of poultry meat is growing as rapidly in Kaliningrad Oblast as in Russia at large. One major issue is deterioration of polders. Much of the oblast, like the Netherlands, is below sea level, protected by dikes, and drained by a system of tiles, canals, and pumps. Some of this infrastructure dates to the 16th century and none of it has been upgraded or overhauled since the fall of the Soviet Union. Putting some of the unused land back into production will require investment of up to USD 1,000 per hectare, though the Oblast government is willing to help with financing some of this work.

¶5. (U) Minister of Economy Lapin described infrastructure projects underway, particularly upgrades of east-west and north-south roads to handle better transit cargo from the Kaliningrad seaport. The oblast has identified five priorities for economic development: producing agricultural raw material for the food processing industry, tourism,

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logistics and transport (the warm-water port coupled with roads), export-oriented manufacturing, and innovation development. Lapin dwelt at length on the six-year holiday on corporate profits (following by a 50 PCT cut in profit taxes in years 7 through 12), and Kaliningrad's Special Economic Zone status that will exist through 2031. Oblast Tax Inspector Aleksandr Fedorov extolled the virtues of the single agricultural tax of 6 PCT (a national, not local, policy) plus relief from VAT and corporate income tax available to investors in the Oblast.

TAXES AND BORDER CROSSINGS

¶6. (SBU) Following Governor Boos's presentation, the floor was opened for questions and answers. The first questioner, a local farmer, asked why individual farmers had been excluded from the list of enterprises eligible to import inputs free of customs duty. Joint-stock companies, she pointed out, can import grain combines and tractors duty-free, but individual farmers cannot, and thus get stuck with 18 PCT VAT plus 5 PCT import duty. Boos promised to look into it and see what could be done.

¶7. (SBU) Another questioner, the local representative of a German investor already engaged in local agriculture, complained that border crossings for foreigners are a major obstacle. "It creates tension," she said, "what can we do to fix the problem globally?" Boos tried to dodge the question, answering that getting goods and products across the border is an enormous problem, but the questioner interrupted. "I'm not talking about products, but about people," she said. "Yesterday it took seven and a half hours for one of my investors to cross the border." Boos again tried to dodge the question, lamely saying it is a problem of lack of "synchronization" with the Polish border guard service, but

is being discussed at the federal level between Russia and the European Union. "We should be better integrated with the European market," he said, "but for now we are temporarily excluded. We are working with the President to propose to the EU making Kaliningrad an open zone," he concluded. Later, another oblast official told AgMinCouns the border crossing issue is Kaliningrad's single biggest headache, and one that the governor simply cannot deal with since it is in the hands of federal authorities, not his.

18. (SBU) A German farmer already vested in an operation in Kaliningrad mumbled to AgMinCouns that the entire dialogue was nonsense, that border crossings are getting more and more difficult -- and not because of the Poles. Damir Imamovic, vice president of Produkty Pitaniya (which has invested USD 112 million in Kaliningrad so far, and intends to invest another 200 million in 2006), stated in his presentation that border crossings remain hard, and since his firm ships 15,000 metric tons of product monthly, all by truck, the time wasted crossing the border is a significant cost.

AUDIENCE

19. (U) The standing-room only forum exceeded the expectations of its organizers in terms of turnout. Over 150 invitees actually came. Of them, 64 were from Germany, mainly Mecklenburg-Vorpommern, Brandenburg, Saxon-Anhalt, and Schleswig-Holstein, and 21 from Belarus. They and a sprinkling of Scandinavians, Poles, and Lithuanians represented both agricultural producers and processors, plus a few input suppliers.

BRINGING THE GERMANS BACK?

110. (SBU) The following day Minister Romanov led much of the group in two large buses around a series of farms, including the impressive Georgiyev Horse Farm, to show what Kaliningrad agriculture is capable of producing. He invited AgMinCouns and German AgAtt Judith Kons to ride with him, and during the course of the day Kons asked him bluntly if inviting Germans to come back to Kaliningrad would not create political problems for him. Romanov admitted that it will, as the idea of letting German farmers come back to "Koenigsberg" after

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over a million Soviet soldiers died to capture it will rub many nationalists the wrong way. Kaliningrad has no other choice, he said. We need the foreign investment, we need the know-how, he had discussed it with the governor, and they had concluded it was worth the political heat from Russian nationalists to invite the Germans back. Otherwise, he said, in another ten years the land currently idle will be so far gone it will never be brought back into production. He added that this new, positive attitude toward foreign investors is a change from the previous governor's policies, and expressed the hope that the agribusiness forum would be only the first of a series of such activities intended to attract foreign attention to the oblast.

COMMENT

111. (SBU) Agronomically there is no reason Kaliningrad Oblast's agriculture could not be put back into production. The critical issues will be market access in the EU for the crops the oblast can produce (mainly rapeseed, some small forage grains like barley, and perhaps some specialty crops) coupled with willingness of foreign investors to pick Kaliningrad over other candidates for investment, such as Poland. Other obstacles are common to Russia as a whole, and include the continued muddle of who owns the farmland, the

fact that foreigners are only permitted to lease land and not to own it outright, shortages of competent local staff to manage and operate farms and companies to Western standards, and shortages of credit for farming operations. The Kaliningrad Oblast administration appears acutely aware of these headaches and to its credit is actively looking for ways to deal with them.

¶12. (SBU) The border-crossing problem cannot be minimized. As an "exclave" cut off from the mainland and now surrounded by the European Union, Kaliningrad Oblast will have difficulty developing tourism as well as attracting foreign investors if visitors truly have to spend an entire working day in line each time they cross the land border. This problem is acknowledged, at least tacitly, by the highest levels of the oblast administration. At the conclusion of the VIP dinner following the forum, AgMinCouns overheard Vice Governor Shalimov assure Prunskiene that he had spoken to appropriate border guard authorities and ensured that her overland crossing back to Lithuania the next morning would not cause her any delays.

BURNS